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KENNETHPORTER

Foreseeable Wealth & Income Beyond Wall Street

The Little-Understood Uses of Properly Funded Whole Life Insurance

Helping Ensure That The Retirement Phase is Profitable & Predictable

MAKING LIFE INSURANCE *SANE, SOUND, & SIMPLE.*

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semper fidelis

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Background & Groundwork

Before you get deep into this white paper I have written, allow me to state the obvious. Using life insurance for any other purpose but its death benefit seems like a strange idea. I know that's how I felt when I first entered the financial services industry 27 years ago and was exposed to alternative options by an economist that taught me to look at the multiple uses of life insurance. I like most consumers understood the overarching reason you would "normally" purchase this product – for the death benefit. To me it was just simple… insurance was insurance. I would only use insurance to transfer the risk of dying too soon. I paid a premium, and some sort of benefit existed should a certain event take place… aka death. It was simply a transfer of mortality risk. Then the question was asked, "If one can transfer the risks associated with saving, investing and income distribution in the pre-retirement and retirement phase should not an individual consider how to accomplish that… even if it utilizes the use of a specific type of life insurance product?" With that sole question in mind I have written this brief with the desire to help you understand how that question can be answered for those researching the alternative uses of life insurance in an overall accumulation, distribution and legacy strategy.

The information that you will find in the following brief focuses on how to employ the properly structured cash value in a whole life policy to maximize various opportunities that you might face over your accumulation, distribution and legacy phase of life. For reference, my firm encounters folks who already own whole life insurance but don't fully consider how their policy may provide an advantage when making various financial maneuvers, and this is unfortunate. The information that follows here is not intended as an introduction to whole life insurance, and it takes for granted several key understandings you might not have if this is your first glance into whole life insurance. This is not a beginners guide and some terminology or depictions might confuse those who don't have an introductory understanding of whole life insurance. If this is you, we invite you check out our other resources and reference material on the subject to gain a fuller understanding of this uniquely designed financial product. It is the case that some life insurance policies have much more to offer than just a death benefit should the insured under the policy die. This brief seeks to highlight the most important of these offerings by focusing on a few unique features of a maximum funded whole life insurance policy.

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Background & Groundwork

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While there are many features and benefits to properly funded life insurance, we are only focusing this brief on the use of life insurance as an alternative or supplement to income / cash-flow distributions in your personally defined retirement phase. Whole life insurance can act as a viable tax-free retirement income benefit and become a powerful asset to complement the rest of an individual's wealth accumulation and distribution plan. Sadly, too many advisors miss the boat on having their clients review this as an option. Many client's ask me why other advisors did not show them these insurance options. My primary belief is they did not discuss the alternatives simply because they did not understand how to do so. Two, others who had an idea were maybe afraid of being viewed as an "insurance salesperson" when assisting you in developing a retirement plan or strategy. Lastly, the small pessimistic voice in me says, "they are aware" but did not want to show you an income strategy that uses an alternative to investment portfolios for the potential reason it could possibly create a reduction in fees to the advisor and/or institution. Whatever the reason, the great news is that you are here today learning a new way to potentially maximize your retirement income - while simultaneously reducing investment risk and picking up additional benefits of tax deferred growth, tax free distributions, additional long term care benefits and ultimately a death benefit that transfers upon your death to the beneficiary of your choice, income tax free! In order to keep this information digestible and brief I will focus my writing on two cash value features of life insurance. First, the benefit of using life insurance as a tax-free retirement income benefit. Second, using life insurance to buffer volatility during the distribution phase when drawing from an equities / stock portfolio. Let's first take a look at the option of using it as a retirement income benefit.

For years, most financial advisors were taught how to accumulate assets, but never how to use those accumulated assets to actually provide clients with an income in retirement. In truth, many, if not most Americans had no absolute need to turn so-called "retirement assets" into retirement income. Pensions still provided strong cash flow in retirement, and this led to elective retirement savings account balances remaining largely untouched. Those days are, for better or worse, in the rear-view mirror and now most people have to figure out how to turn their wage-earning efforts into retirement income success or else suffer the consequences of living in poverty during retirement. Whole life insurance can play a unique role in the effort to generate retirement income because it boasts a few distinct features that make it strong at accomplishing this goal:

- Enjoys incredible tax benefits
- Produces a very attractive return and yield on investment
- Offers very stable year-over-year returns
- Enjoys versatility unmatched by other retirement income-focused options

Tax Benefits

Whole life insurance enjoys a long history of extreme tax favorability. These benefits were deemed so favorable that Congress intervened in the 1980's to pull back some of the advantages whole life insurance had because they were viewed as too easily abused in the pursuit to avoid tax payments. The "intervention" came in the form of life insurance qualification testing and reclassification in the event of failure that strips life insurance of its tax advantages. This, of course, lessened the power of whole life insurance as a tax-free cash accumulation vehicle, but it by no means completely ended the practice. So long as life insurance is designed and implemented correctly to operate within the parameters set forth by the law, it maintains its favorable tax treatment. The main tax benefits life insurance enjoys (especially in the context of retirement income) are:

- Tax deferred accumulation of cash values
  - This means gain earned on cash values in a whole life insurance policy do not carry a tax liability in the year earned. Unlike, for example, a savings account where interest payments carry an income tax liability in the year the interest is earned, whole life insurance cash values grow with no 1099 sent at the end of the year.
- Recoverable basis prior to distributing gain
  - The accounting term for this is FIFO or First In First Out. It means your client can withdraw their non-taxable basis (i.e. the money paid into the policy and theoretically already paid income taxes on) from a whole life insurance policy first and then once all of the basis is gone you can will distribute gain (which is taxable as ordinary income) from the policy.
- Tax free distribution of gain (provided it is taken as a loan)
  - To avoid paying taxes on the gain distributed from a whole life policy, one simply uses a policy loan, which carries no taxable consequence because this distribution is treated as a loan not an actual distribution from the policy.
- Classification of Dividends as a Refund of Premium
  - While some use this special classification of dividends as a way to speak negatively about whole life insurance, this is a powerful bonus to whole life insurance policyholders. It means the dividend payment does not carry an income tax liability in most cases like dividends from a stock company do.
- Tax Free Death Benefit
  - While the intention of this book isn't really to talk much about death benefit, the tax free status of a death benefit can be extremely powerful for retirement planning as it generates substantial non-taxable assets for a surviving spouse and also helps policyholders access certain other assets without worrying about child inheritance or legacy planning.
- No Impact on Modified Adjusted Gross Income (MAGI) or Most Other Income Qualification Tests
  - Life insurance distributions taken as a withdrawal to basis and policy loans on gains do not affect the calculation for MAGI, nor do they typically affect income qualification tests for other government programs. This means that using whole life insurance distributions as a source for retirement income do not affect the taxability of social security income.

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If you Like Predictable Returns and High Relative Yields.. This Could Be For You

1. The income whole life insurance can generate is impressive, and the tax-free nature of this income greatly increases the net return on investment. Let's look at a scenario to quantify what whole life insurance can offer. The example below shows a 40-year-old male. If you are older than 50 do not stop reading here. Do not be dismayed if you are in your late 50's, 60's or even in your 70's. If a policy is properly structured for cash accumulation, you will be able to create an income strategy and develop a buffer against stock market volatility… even if you are later in life. When a prospect / client is older we will compress the premium payments into shorter period utilizing the lowest death benefit as to not violate the modified endowment contract limit set by the IRS.
2. To learn more about how we would fund a life insurance contract following the IRS guidelines for whole life insurance please contact our office. You can use this link to schedule a review https://calendly.com/kpandco/client-advisor-topic-review

John is a healthy 40 year old male who plans to put **$25,000** per year into a whole life policy until he turns 66 and then use the life insurance contract for retirement income beginning at age 66 through the rest of his life, which he will plan to last through his age 100.

$25,000

The whole life insurance policy projects an income distribution of **$64,000** per year from 67 to 100. This represents 12.40% yield on investment.

12.4%

The top pick among High Yield dividend funds according to fool.com was:

3.8%

When John was 80, his whole life policy achives a compound annual growth rate of 5.5% per year.

5.5%

Amount of money going in

$25,000 per year.

2

Number of years premium going in

26 YEARS

Income distribution start at age

67 **$64,000**

per year until age 100

4

Number of years for income

33 YEARS

Total income generated

$2,112,000

Stability is *"Boring"* / Volatility is *"Exciting"*

I have visited Bush Gardens many times with my children and grandchildren over the years. As a young man I can remember getting on the Loch Ness Monster numerous times a day while at the park. It was a ride of exhilarating turns, twists, dips and loops. I later shared this experience with my children, but something changed as I aged. My tolerance for dips and loops just didn't agree with my stomach. I am sure many of you can relate to the physiological changes that come along with aging. Present day, I have relented to the "kiddie rides" with the grandkids at the park. Boring park rides work for me just fine these days. I still enjoy Bush Gardens, time with my family and smooth park rides. My need to feel the excitement of going up the hill only to feel a roller-coaster ride that plunges 220 feet to earth at 70 miles per hour is no longer my idea of excitement. There is a similar feeling and tolerance that also exists in the world of investments. I will address this in further detail under smoothing volatility. I want to state what may not be obvious to many about whole life insurance… it's the "boring ride" at the park. It's returns fluctuate very little, and it certainly isn't going to hold a captive audience at your next cocktail party with your guests listening to you pontificate about the exciting world of whole life insurance. But boring also means stable, and stability has a way of being highly coveted, especially as experience and time in the market progress. Especially, when one starts the systematic withdrawal of income from an investment that has variable returns to include negative returns on investment. Young investors are not immune to financial roller-coaster rides either. They simply have a longer glide path to recovery before the next ride (correction in the market) occurs. In the same sense that young people often believe they will never get sick and need physical assistance, many younger Americans naively believe their finances will avoid a similar fate. I have had the opportunity to observe the aging process with many prospects / clients over the last 27 years and can attest that age brings fragility both physically and financially. Fortunately, whole life insurance policies tend to strengthen over time and what they have to offer is a wonderful complement to an aging and more precarious financial circumstance. In absolute transparency, the change in whole life returns is rather slow and uninteresting. Our own data shows that while dividend rates can and do change, they do not change substantially even over decade long time periods. This lack of up or down volatility might cause some to dismiss whole life insurance because it lacks sex appeal. If you need to live a life in the fast lane, whole life insurance might cause you a bit of anxiety because it doesn't produce a thrilling ride. But if you're seeking a more reliable product, one you can predict with some degree of accuracy year-over-year, then a properly designed and implemented whole life insurance policy has a lot to offer.

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Adaptive Function of Whole Life

The tax benefits enjoyed by *whole life* insurance are unique for a financial product that is not bound by additional time sensitive or event specific requirements. Think in terms of IRA's or 401(k)'s. Both have generous tax benefits, but both also restrict access to funds for the majority of a client's life. On top of this, both accounts can force them into unwanted liquidation at a more advanced age. What we are eluding to is the 59 ½ rule as well as Required Minimum Distributions now starting at age 72 thanks to the SECURE Act. *Whole life* insurance funds are accessible at any time and for any reason. One need not achieve a certain age, nor require proof of a hardship to remove money from the policy without penalty. Additionally, one can age without worry about forced liquidation of the account. This gives *whole life* insurance a leg up for various retirement planning scenarios, but a major application is early retirement. While there are various provisions of the U.S. tax code that do permit penalty free liquidation of IRA's and 401(k)'s prior to age 60, this is not without restriction and not without a requirement for administrative exactitude. *Whole life* insurance lacks all of these burdens. It's also worth understanding that the tax-free nature of *whole life* insurance income creates additional versatility that removes restrictions one might face for account liquidation out of fear of tax consequences. Consider an individual who wants to use IRA money to make a car purchase so that they can save on the interest paid for an auto loan. Withdrawing the money from the IRA might bump him into a higher tax bracket or create a higher tax liability for Social Security income. When you make a distribution or withdrawal / loan from *whole life* insurance comes with no such concerns.

Smoothing Volatility in the Income Distribution Phase

Think back on how you have behaved or the feelings you had when markets started to fluctuate, much like those feelings you experienced on the rollercoaster rides at Busch Gardens. It has been my experience over almost three decades in the financial services industry that when markets start to show weakness investors will likely be bombarded with panic induced headlines. Over reaction is often the consequence, with investors abandoning previously developed investment strategy and investment plans. Ultimately fleeing to the safety of cash or fixed investments out pure fear versus a methodical well-planned financial strategy. Financial professionals know that moving out of the market means no chance of participating in any rebound and therefore less chance of recouping losses experienced in the fall. So how can I encourage my clients and prospects to weather the storm and stay invested when volatility rears up? Diversify your investments with non-correlated assets like max funded *whole life* insurance as well as other non-correlated assets like home equity, fixed annuities and fixed index annuities. We will discuss in further detail the use of home equity, reverse mortgages and annuities in a follow up paper. When many clients hear “diversification”, they think of a portfolio including a mix of stocks and bonds. But even within an equity portfolio spread out across multiple asset classes, there’s still some correlation between returns; when one investment falls, others are likely to as well. *Whole life* insurance is a masterful product to utilize inside your investment process to smooth volatility in the income phase.

• THE AVERAGE S&P 500® ANNUAL RETURN IS APPROXIMATELY 8%. THE AVERAGE 1-YEAR RETURN FOLLOWING THE LOWEST POINT OF EACH BEAR MARKET IS 47%.

• HISTORICALLY, BEAR MARKETS HAVE OCCURRED AN AVERAGE OF ONCE EVERY 6 YEARS.

• 50% OF THE S&P 500®’S STRONGEST DAYS IN THE LAST 20 YEARS OCCURRED DURING A BEAR MARKET.

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Smoothing Volatility in the Income Distribution Phase

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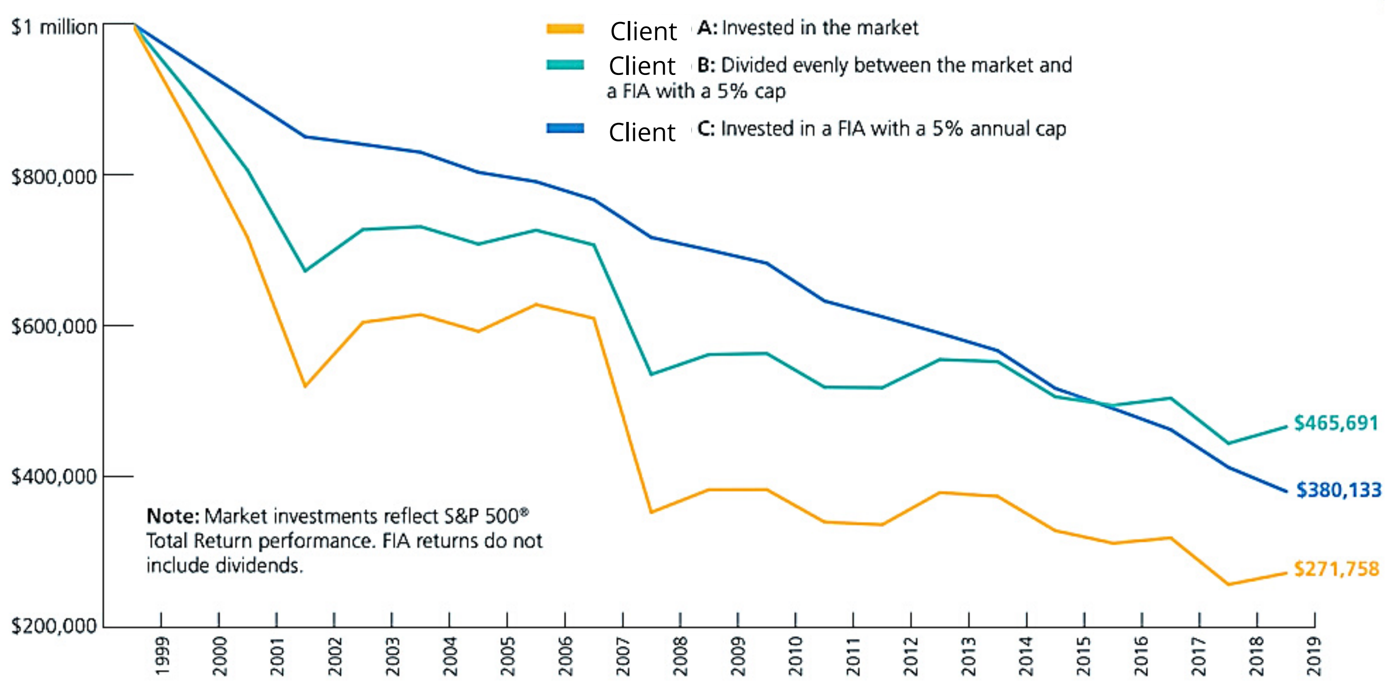
Whole life insurance that is properly funded for early and maximum cash accumulation can serve as buffers against market swings and downturns. With a whole life policy, policyowners are guaranteed to experience growth in their cash value, even when markets fall, and there's no direct correlation to equity market performance. And when dividends are reinvested and used to purchase additional coverage, these policies have the ability to increase their cash value accumulation potential free of taxation. With a death benefit that's also increasing, the policy holder is building up protection not only for their future needs, but also for their loved ones simultaneously. Growth during market declines is an obvious benefit to clients, but where whole life policies truly shine is their ability to turn that growth into usable assets. Whether it's used to support a small business, pay college tuition for children, provide retirement income or any other purpose, policy owners can access the cash value that's been built up in their policy over time via tax-free withdrawals of the basis and / or policy loans. And if clients choose to do this while the market rebounds from a downswing, it can give their assets tied to equities the ability to participate in the recovery. To demonstrate this point, we'll compare three hypothetical clients who wanted to generate income. All three client accounts are represented by an initial $1 million market investment and each portfolio provides $50,000 of annual income



Smoothing Volatility in the Income Distribution Phase

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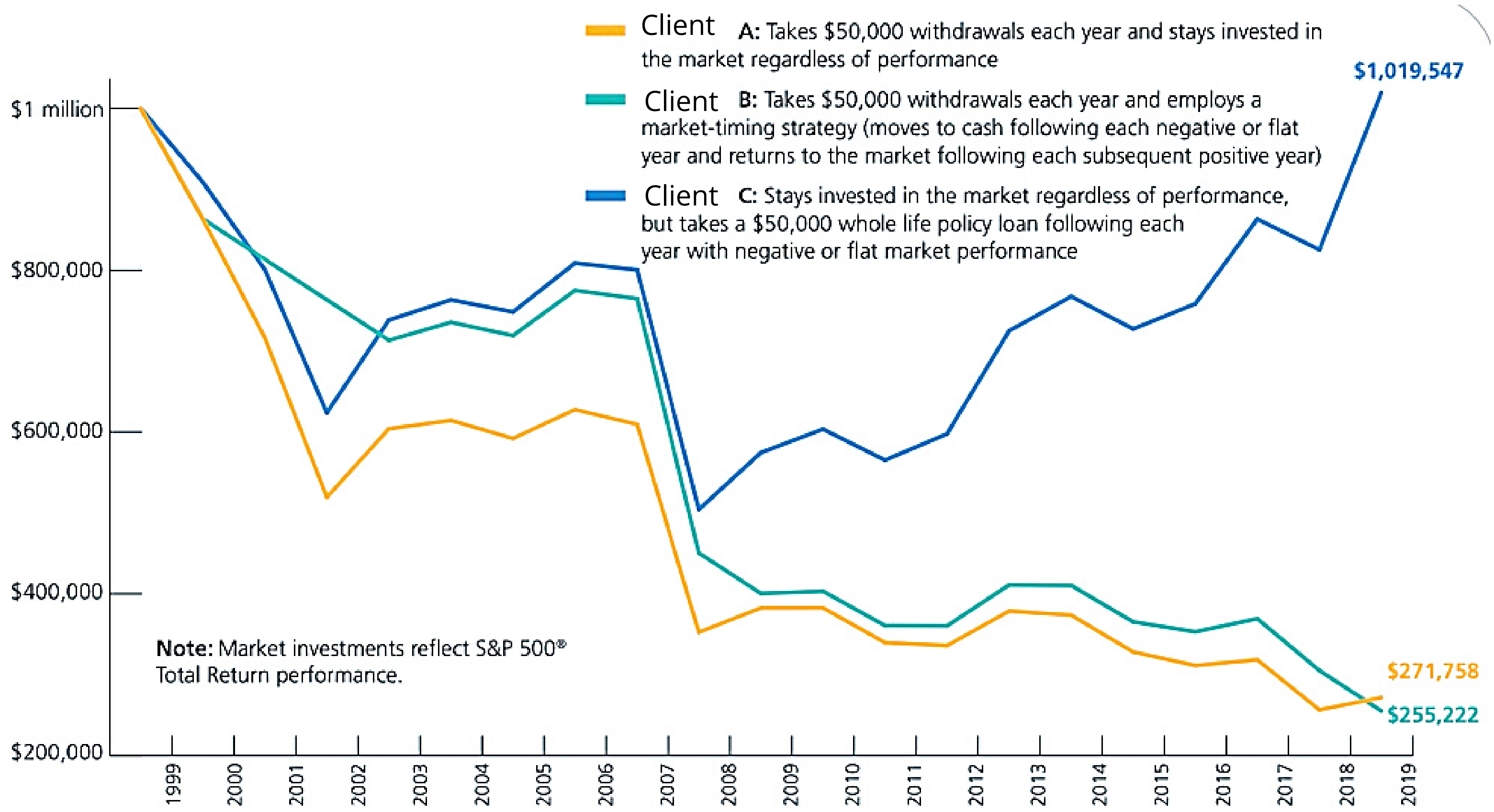

These results are based on the last 20 years of S&P 500® returns, and the difference between the experiences is dramatic, with Client C's value at the end of this period even higher than the original investment. Withdrawals from assets tied to equity markets during or following a downswing act as a ***double whammy***, with both events reducing the overall value and leaving fewer assets to build from when markets recover. In this example, market-timing strategies fared as expected missing out on the growth opportunities associated with market rebounds. Whole life withdrawals through surrender of basis and / or policy loans can reduce or eliminate the need for income withdrawals from assets in the market, letting our clients stay invested and dedicated to their long-term investment strategy. In fact, according to Dr. Wade Pfau and Dr. Michael Finke, a retirement income strategy that included whole life insurance as a buffer against volatility was more efficient and offered more overall income throughout retirement. (If you would like to read the full study by Dr. Wade Pfau and Dr. Michael Finke please reach out to the ***KP&Co Team*** and we will provide you a copy of the study.)

Closing Comments and Disclosures

Make no mistake, insurance products aren't an overnight fix for volatility. They aren't intended to be. Whole life policies take time to build up their cash value. FIAs have surrender charges that typically last for a five- to ten-year surrender period and reduce the amount of income available in the early stages of the contract by applying penalties for excess withdrawals. The examples go on, but the point remains the same: these are long-term products, many of them intended to provide benefits for a lifetime. But sudden, unexpected market drops are the perfect opportunity to remind you of the importance of long-term strategy and the critical function properly funded whole life products can serve. Most investors will experience multiple bear markets or corrections during their life and buying whole life insurance today is a strategy that can help soften tomorrow's market blows. Conventional wisdom tells us we need to pay attention to market cycles rather than each individual peak or trough, because when the market falls, it's often followed by a strong rebound. We want to make our clients more resilient to losses and swings with a focus on the process of wealth creation, rather than short-term returns and one financial products strength over another. Long-term goals are exactly what whole life insurance products are designed to address. It's not a get rich quick scheme. The wealth planning process is critical to prepare for market unknowns. A portfolio that relies entirely on the market is much more vulnerable to volatility than one that features multiple products inside an efficient financial process with each product offering varying degrees of performance, correlation and protection features. Volatility simply isn't as frightening when guarantees are in place to protect portions of a portfolio and reduce its total risk. Properly funded whole life insurance can provide stability that makes a portfolio resilient, or its ability to improve smooth the glide path of income distribution. The unique features whole life insurance is the key component to smoothing out the impacts of market volatility.

We anticipate this paper will help many prospects and our current clients gain understanding and comfort with whole life insurance, which in turn will strengthen their ability and willingness to discuss whole life insurance with me or any trusted advisor that understands the value of owning properly funded whole life insurance. In fact, it's the primary reason we set out to write it. To help our clients understand better and reinforce the value of a properly funded whole life insurance policy designed for retirement income distribution purposes. From time to time prospective insurance buyers will effectively ask us to tell them everything we know about whole life insurance. We know it's an honest attempt to understand all the highs and lows as quickly as possible. In true transparency, we've never successfully executed on this request. This isn't due to lack of effort or an unwillingness to share this information. The truth is the subject is far too large to neatly impart every crucial detail. We bring this up as a warning. Reading this paper will certainly advance your knowledge on this subject, but it by no means gives you everything you need to know. The subject of whole life insurance spans several considerations beyond just how one can use its cash value to reap benefits. What you have read by now gives you a solid understanding of two key components of using life insurance in an income distribution plan. We don't seek to shake your confidence, rather we want you to understand what more you can accomplish by understanding a little more about the uses of max funded whole life insurance.

NEXT STEP

Do you want some help understanding how to possibly implement max funded whole life insurance in your financial strategy?

Please send your questions and concerns to: team@kennethporterandco.com Someone from our team will respond within 24 hours if you send your request Monday - Friday. If you send a message over the weekend, we'll get back to you on Monday.

If You Want to Hire Us for Private Consulting?

We're available for one-on-one private consulting with prospects, clients even other agents or other financial professionals that want to learn how to implement properly funded whole life insurance into your plan (or your financial practice if you are an advisor).

1. Prospects who only want a policy review / analysis can schedule a complimentary review by contacting us at: team@kennethporterandco.com or at our office 757.955.8071.
2. You may also click this link to our calendar to schedule a review https://calendly.com/kpandco/client-advisor-topic-review
3. For financial professionals we will hold training classes (by webinar, Zoom or live events), policy review/analysis, and helping advisors figure out where life insurance may fit into one of their client's financial plans. We're happy to discuss any of those options with you. Our firm's hourly risk review and insurance consulting starts at $450/hr. We are open to consulting for a firm fixed price as well as case splits. If that's something you'd like to discuss just reach out with your questions and comments at: team@kennethporterandco.com